

State of Montana 2007 Legislative Session
Testimony before House Taxation Committee
April 11, 2007

EXHIBIT 1
DATE 4.11.07
SB 138

Mr. Chairman, Members of the Committee:

I appear before you this morning as a proponent of Senate Bill 138 sponsored by Senator Wanzenreid. The Bill closes a loophole in the tax laws which govern the taxation of insurance companies which has allowed certain individuals and corporate entities to form and over-capitalize small insurance entities as a way to avoid paying capital gains and investment income taxes that would be otherwise due to the Federal and State Governments.

When first proposed, Senate Bill 138 created significant concern for us at ALPS and the industry as a whole. However, ALPS Management and Governmental Affairs Personnel developed a very constructive dialogue with Senator Wanzenreid and the Department of Revenue who considered the risk that the bill might impose on legitimate operating insurance entities and made appropriate amendments to address most of the issues we raised. As this bill stands before you, it now only represents a slight risk to inactive companies and those which may be winding down certain books of business. That being said, I believe that the current Montana Tax Code and this bill contain sufficient appellate rights and processes to allow dormant companies and those running off certain books of business to be protected by a reasonable assessment of the entities intent and the consequences of imposing law created by this legislation.

Prior to 2006, IRC section 501(c)(15) provided an exemption for small insurance companies like many of the county or farm mutual companies that exist in Montana from federal taxation if their gross premium level was less than \$350,000. In short, they paid no federal tax and were taxed at the state level appropriately under existing premium tax laws. Unfortunately, this allowed for abuses as individuals and corporate entities figured out that they could form captives and small insurance companies that collected very little insurance premium but were packed with significant assets, as a tax dodge; they produced significant non-premium income all of which was not taxable at either the federal or state levels (premium tax being the sole tax revenue source at the state level). At the Federal level Congress and Treasury have plugged the loophole in IRC section 501(c)(15) so that it no longer provides an exemption based solely on premium income. Rather, it now provides a larger exemption of \$600,000 but applies it to both premium and investment gain and income of both the small insurer and any parent or affiliate. Thus, it now appropriately applies, as originally intended, to small county or farm mutual insurers with legitimate insurance interests that provide significant benefits to small business, property owners, farmers and ranchers.

This bill should not be seen as an anti-insurance industry bill as legitimate operating insurance organizations have adequate protection from being netted by the impact of this bill.

Respectfully submitted,
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President & CEO
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